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The Director of Central Intelligence

Washington, D.C. 20505


National Intelligence Council

NIC 01317-85  
11 March 1985

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MEMORANDUM FOR: Director of Central Intelligence  
Deputy Director of Central Intelligence

FROM:

  
Acting Intelligence Officer for Economics

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SUBJECT: Japan Trade: Meeting of Senior Ad Hoc  
Group on International Economic Policy

1. On Saturday morning, 9 March 1985, Secretary Baker convened a restricted ad hoc group (i.e., less than the full SIG-IEP) to continue discussions on strategy for the current trade negotiations with Japan. The meeting was attended by Secretary Shultz, Secretary Baldrige, National Security Advisor McFarlane, and others.

2. After lengthy discussion, the following general conclusions emerged:

- Historically, US trade negotiations and trade policy have been based on the concept of "national treatment," which in this case would mean that US producers must be treated as well in the Japanese market as the best-treated Japanese firms. It was concluded that the treatment of US firms in Japan is discriminatory. However, we cannot alter our trade policy to insist on the alternative concept of reciprocal treatment, i.e., that US firms must find it as easy to sell in Japan as Japanese firms find it to sell into the US.
- It is important that progress be made in these negotiations by April 1, in the case of telecommunications, and by the May Bonn Summit in general. It is also important to defuse the rising political pressure

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SUBJECT: Japan Trade: Meeting of Senior Ad Hoc Group on International  
Economic Policy

in the US on this issue. Accordingly, the US must define specifically what we consider necessary to obtain from Japan (our "bottom line") and convey this to Prime Minister Nakasone promptly.

- State (Wallace) was tasked to put into letter form the US position for telecommunications and Treasury (Mulford) was tasked to summarize the US position on the other three sectors. Mulford was given the latter task by default since so many of the primary players in USTR and Commerce were on their way to Japan.
- The telecommunications position is to be based upon the letter dated 5 March 1985 from Lionel Olmer to Vice Minister Koyama (copy attached).
- The positions are to be formulated and reviewed during Monday and Tuesday, March 11 and 12. It is then likely that Gaston Sigur of the National Security Council Staff will be asked to convey these positions to Prime Minister Nakasone personally and privately.
- Papers were submitted to the meeting on the NTT Agreement and the US-Japan Civil Aviation Negotiations (copies attached). The meeting did not focus on these items in detail, but in general terms US policy will be to take a tough line on these issues throughout March in order to maintain pressure on the trade negotiations, but without specifically linking these issues to the sectoral negotiations.

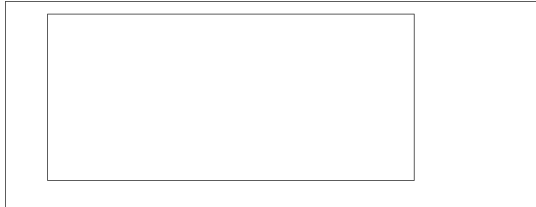
3. USTR has thoroughly involved representatives of the affected US industries, and it was recognized that one of the most important shortrun measures of success in this area will be the perception of the affected US industries that they can live with what is negotiated.

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4. Any interagency review of the sectoral position papers is likely to be very selective and informal. Secretary Baker tentatively set 19 March as the date for another review of the status and progress of the negotiations and US strategy.



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**Attachments:**

- A. Letter from Olmer to Koyama
- B. NTT Agreement
- C. U.S.-Japan Civil Aviation Negotiations

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ATTACHMENT A

Tokyo, Japan

March 5, 1985

The Honorable Moriya Koyama  
Vice Minister  
Ministry of Posts and  
Telecommunications  
1-2, Kasumigaseki 2-chome  
Chiyoda-ku, Tokyo 100

Dear Vice Minister Koyama:

I want to thank you for the time and the great effort that you and your staff have given to our mutual efforts to discuss the application of Japan's new telecommunications law which becomes effective on April 1, 1985.

I believe that our efforts have resulted in some progress, although I am sure that you agree we have much further to go to resolve all problems.

I am sure that you share my desire that Japan create a telecommunications environment as free of unnecessary barriers as is possible. It is in the interest of achieving this objective that I make these comments, for my own careful review of our mutual efforts to date reveal that, if left untouched by your personal intervention, a system will be put in place beginning on April 1, 1985, which seriously disadvantages foreign suppliers, does an injustice to Japanese consumers and lends fuel to an international perception that, despite political statements to the contrary, Japan remains committed to keeping its market essentially protected from foreign competition.

Our two governments have been discussing some of the outstanding issues in the telecommunications sector for more than a year. This is particularly true of the issues concerning the notification and registration of Type II telecommunications enterprises. A year ago, the U.S. Government pointed out, in the strongest possible terms, that registration and notification procedures could become barriers if they were to include a prior approval process.

At that time, your Government provided assurances that such procedures would be simple and automatic and that applications would be rejected only in very unusual circumstances to be established by law.

However, after examination of the actual law and discussions with your Government concerning the pertinent Cabinet and Ministerial ordinances, our original concerns have become amplified. The proposed procedures require a great deal of seemingly unnecessary information and, in instances, business-confidential data; they also appear to contain an obligation to obtain prior approval at various levels of the Japanese Government.

Accordingly, I hope that, as a result of our discussions, you will be able to simplify the procedures and to make them automatic and, thus, eliminate the need for prior approval. Also, to ensure transparency, I propose that you create an appeal channel and periodically review established procedures.

I believe that you also are aware that we have been concerned for some time with the distinction between "general" and "special" Type II telecommunications enterprises -- specifically, the use of 500 lines and 1200 bits per second (BPS) as one of the criteria to distinguish between the two categories. We believe that the use of this criterion may impede technological development within Japan's telecommunications sector. For example, how will your Government handle the classification issue when, in the very near term, the use of fiber optic systems increases dramatically in Japan?

Similarly, we are concerned with the definition of an "unspecified" number of customers which also will serve as a criterion to distinguish "general" from "special" Type II enterprises. I hope that you will be able to define "unspecified" more clearly and to confine such a criterion predominantly to voice transmission. As with the 500 lines/1200 BPS criterion, it would be preferable not to use an arbitrary, numerical calculation to determine the meaning of "unspecified."

In the area of standards and certification, you know that we are concerned with the potential for trade barriers to arise in the future. To avoid potential problems, I believe it is

essential that only one independent approval agency be responsible for certifying all "customer premise equipment" for attachment to all telecommunications networks. This means that NTT would not have the authority to certify equipment for itself or for any other company.

I also believe that, in accord with the GATT Standards Code and the Gotoda Commission Report of 1983, MPT should provide ample opportunity for comment on the draft standards and rules for approving equipment, which were made available only last week.

Regarding the standards, they should be established solely to prevent harm to the network.

Another issue of longstanding concern is the potential for cross subsidization between communications services that will be offered by NTT after April 1, 1985. I know that you also are concerned about this problem. I trust that you will do your best to prevent any such possibility through the establishment of strict accounting and other procedures within NTT. Safeguards against cross subsidization within NTT should be guaranteed in order to ensure full competition in the new telecommunications environment which you are creating. We have provided your staff with a listing of specific measures to guard against cross subsidization, based on our experience with telecommunications development in America.

Finally, there remains the question of representation on advisory councils. This difficult issue has been addressed in other bilateral discussions. I understand that the members of a council are chosen for their experience in and knowledge of a particular sector. Accordingly, Japanese nationals working for foreign-affiliated telecommunications companies in Japan should have an opportunity to bring their special knowledge to advisory councils which consider telecommunications issues. Therefore, I urge you to provide for membership for such persons on all relevant advisory councils.

I would also like to point out that under the U.S.-Japan High Technology Agreement of 1983, Japan agreed to make efforts to ensure that the representatives of such foreign-affiliated companies serve on all committees which develop policy or draft standards in the high-technology field. I trust that you will ensure that this commitment is met in the telecommunications sector.



An objective within my government has been to write laws, and the regulations for their implementation, which limit to the maximum extent possible the discretionary authority of personnel in the agencies charged with their administration. One reason for this objective is to provide the private citizen falling under these laws with the maximum degree of certainty and predictability and to reduce his dependency on the whims of bureaucrats who can often interpret laws to suit transient interests. My feeling on the development of your implementing directives is that they do not yet go far enough in the direction of limiting discretionary authority. I believe firmly that they must, if we are to achieve our objective of an open telecommunications market.

I am looking forward to our working together to promote competition and innovation in this most vital sector which links our two countries. However, time is growing short and it is obvious that the pressure on both of us to succeed is intensifying.

Sincerely yours,

Lionel Olmer  
Under Secretary of Commerce  
for International Trade

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ATTACHMENT B

NTT AGREEMENT

The NTT Procurement Agreement has two elements: (1) Japan placed NTT's non-telecommunications system purchases under the Government Procurement Code, and (2) Japan agreed to apply the Code on a bilateral basis to the remainder of NTT's purchases. In return, the United States agreed to apply the Government Procurement Code to Japan. We insisted on the full opening of NTT as a quid pro quo because it is the only way Japan undertakes obligations comparable to the benefits we provide by opening the USG procurement market to Japan.

The original three-year Agreement ran from January 1980 through December 1983. The Agreement was renegotiated with improvements and signed by Ambassador Brock and Foreign Minister Abe in January 1984. The Agreement, which runs for three years, contains an annual review provision. The first year review has been completed. The Agreement will continue in force unless a decision is made to terminate.

U.S. sales to NTT have been extremely disappointing. We have continued the Agreement for three reasons. First, U.S. firms remained hopeful that their efforts to sell would eventually be successful. Second, U.S. firms believe that termination of the Agreement, without also closing our market, will not benefit them commercially and could cost them possible sales to NTT. Third, while the volume of sales was low, the rate of increase was encouraging, from \$15 million to \$40 million to \$140 million over the first three years.

NTT has informed us that procurement for the fourth year, which ends March 31, will drop to about \$130 million.

Option 1: Terminate

Under the terms of the NTT Agreement, the United States can terminate the bilateral portion of the Agreement at any time following notice and consultation. If we terminate the bilateral portion of the NTT Agreement, however, the multilateral element of the Agreement will continue under the Government Procurement Code. We will remain bound to grant Japan the full benefits of the Code in the USG procurement market. Nevertheless, if we terminate the bilateral portion of the Agreement, we face a choice of either accepting an extremely unbalanced deal with Japan under the Code or terminating application of the Code to Japan, which will put us in violation of the Code. As a practical matter there is little that the Japanese could do if we ceased to apply the Code to them. If they decided to initiate a formal dispute against us, the most they could achieve would be authority to stop applying the Code to the United States.

As a matter of domestic law, the U.S. Trade Representative has the authority to terminate U.S. application of the Code to Japan at any time. Under the terms of the Trade Agreements Act, this would result in Japan being barred from bidding on U.S. procurement that is covered by the Code.

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CLASSIFIED BY

3-9-85  
*James M. Murphy, Jr.*

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*USTR Recommendations*

Option 2: Threaten Termination

The USG could notify the GOJ of its intention to terminate because of NTT's unacceptable performance and request formal consultations under the Agreement. We would seek to use this threat to obtain significantly improved performance by NTT.

Option 3: Do Nothing

If the USG does nothing, the Agreement will continue. The GOJ and NTT will likely interpret this to mean that they do not need to continue increasing purchases in order to satisfy the United States unless we make it clear that we will not accept another year of lackluster performance.

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## U.S.-Japan Civil Aviation Negotiations

### Background

Currently, U.S. and Japanese airlines derive approximately the same amount of gross revenues from service operating under the U.S.-Japan Air Transport Agreement. The five U.S. carriers serving Japan earned a total of \$1.15 billion in 1983. Japan Air Lines (JAL) earned \$1.04 billion (including revenues from operations between the other countries in Asia and the United States). Broken down by cargo and passenger operations, the picture is as follows:

Cargo Operations In 1983, U.S. carrier revenues from cargo moving between Japan and the United States totaled \$285 million, versus \$180 million for JAL. Overall, if cargo carried between other Asian points and the United States via Tokyo is included, U.S. carrier revenues substantially exceed those of JAL. (Japan serves as a critical transshipment point for U.S. carrier cargo services; 60 percent of all cargo moving between Asia and the United States on U.S. carriers moves through Japan.) Currently, Flying Tigers operates 26 weekly flights eastbound from Japan to the United States, NW operates 11 and JAL 24. Over 200 weekly combination passenger-cargo flights provide additional cargo capacity.

Passenger Operations In 1983, U.S. carrier passenger revenues totaled \$824 million; JAL's passenger revenues totaled \$692 million. Four U.S. airlines carried 48 percent of the market while JAL carried 43 percent. U.S. airlines operate approximately 120 flights per week while JAL operates approximately 75 flights per week.

Current Negotiations Although comprehensive bilateral negotiations were underway, the Japanese desire to obtain entry for Nippon Cargo Airlines (NCA) on April 1 furnished an opportunity to negotiate a provisional package prior to the conclusion of the comprehensive talks. At negotiations which ended in Tokyo March 2, the two countries' chairmen were discussing, without commitments on either side, the following package of benefits:

Limited entry of NCA up to six flights per week between Tokyo and San Francisco/N.Y. with increases in NCA flights based upon cargo market growth rate.

The elimination of frequencies and aircraft type restrictions on services between Japan and Guam/Saipan with opportunities for new airline operations in those markets.

Opportunity for a total of three new daily services for both sides, phased in, between U.S. cities and Japan.

Provisions eliminating excessive Japanese regulation of U.S. carrier operations.

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### Factors for Consideration

#### Pros

- o U.S. obtains new long-sought service opportunities which would enable U.S. carriers with significant hubs to provide new competitive services to Japan.
- o Elimination of operating restrictions in Micronesian markets which have been source of conflict between the United States and Japan.
- o Removes some historic regulatory constraints on U.S. carrier operations.
- o Furthers progress in U.S.-Japan aviation relations which have gradually improved since 1982.

#### Cons

- o Other than protection of their Chicago gateway and some "doing business" benefits, package contains nothing for U.S. cargo carriers and is subject to criticism for trading their interests for combination/passenger opportunities.
- o All U.S. incumbents are critical of the package.
- o Projected market growth resulting from new services will be influenced by pricing flexibility available, a subject unaddressed in this package.

**EXECUTIVE SECRETARIAT**  
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Remarks

Papers for this meeting are  
expected via LDX between 5-6 p.m.  
tonight.

Executive Secretary

8 March 1985

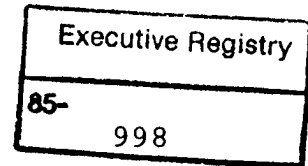
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THE SECRETARY OF THE TREASURY  
WASHINGTON, D.C. 20220



March 8, 1985

MEMORANDUM FOR THE SECRETARY OF STATE  
THE SECRETARY OF COMMERCE  
THE SECRETARY OF TRANSPORTATION  
DIRECTOR OF CENTRAL INTELLIGENCE  
UNITED STATES TRADE REPRESENTATIVE  
ASSISTANT TO THE PRESIDENT FOR NATIONAL SECURITY AFFAIRS  
ASSISTANT TO THE PRESIDENT FOR POLICY DEVELOPMENT  
CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS  
DEPUTY SECRETARY OF THE TREASURY

SUBJECT: Senior Ad Hoc Group on International Economic Policy

A meeting to discuss U.S.-Japan trade negotiations is scheduled to be held on Saturday, March 9, 8:00 - 8:45 a.m. in the White House Situation Room. This meeting will continue the discussion from the March 7 SIG-IEP meeting. Papers will be circulated later today.

  
James A. Baker, III

cc: Staff Secretary and Deputy Assistant to the President  
Deputy Assistant to the President for Cabinet Affairs

MAR 8 1985

